

## **Senate Bill No. 826**

### **CHAPTER 205**

An act to amend Sections 16724.5, 16731, 16731.6, 16735, 16737, 16752, 16752.1, 16753, 16754, 16754.3, 16755, 16757, and 16780 of, and to repeal Section 16736 of, the Government Code, relating to general obligation bonds.

[Approved by Governor October 11, 2009. Filed with  
Secretary of State October 11, 2009.]

#### **LEGISLATIVE COUNSEL'S DIGEST**

SB 826, Committee on Governmental Organization. General obligation bonds.

(1) The State General Obligation Bond Law generally provides for a procedure that may be adopted by other acts, with any necessary modifications, in authorizing the issuance and sale of state general obligation bonds and providing for the repayment of those bonds, including the determination of interest rates the bonds shall bear. Existing law requires, with regard to a resolution specifying that the bonds may pay a variable interest rate, that the aggregate principal amount of all state general obligation bonds bearing variable interest rates does not exceed 20 percent of the aggregate principal amount of all outstanding general obligation bonds. Existing law exempts, from this calculation, variable rate bonds that have an effective fixed interest rate through a hedging contract.

This bill would require the Treasurer to determine, with regard to those bonds that have an effective fixed interest rate through a hedging contract, that the hedging contract either significantly reduces variable rate risk or qualifies for integration with the bonds in calculating the yield on the bonds under certain federal rules.

(2) Existing law provides that certain amounts payable or contractual obligations regarding bonds that bear a variable interest rate under a bond act that was approved by the voters before July 1, 2002, are not backed by the full faith and credit of the state. Existing law specifies that this contractual obligation is under a standby bond purchase agreement or other liquidity facility.

This bill would instead provide that this contractual obligation is to repay advances and pay interest thereon under a credit enhancement or liquidity agreement. The bill would also provide that those amounts payable or those contractual obligations are backed by the full faith and credit of the state, if the bond act was approved on or after January 1, 2002.

(3) Existing law requires, for bonds approved by the voters after January 1, 2006, that the payment of interest include the payment of any amounts owed by a counterparty after any offset for payments owed to the state on

a hedging contract, and prohibits the total payments of stated interest on the bonds and payments owed by the state from exceeding a specified maximum rate after a specified offset.

This bill would instead provide that the payment of any amounts owed by the state, after any offset, shall be deemed to be included within the appropriation for interest on the bonds. The bill would allow the payments of interest on a bond and the payments on a hedging contract that exceed the maximum rate in a fiscal year to be paid in subsequent fiscal years, under specified conditions.

(4) Existing law requires, when the finance committee created by the bond act determines to issue commercial paper notes, for purposes of determining the principal amount of outstanding bonds, that the principal amount deemed outstanding be the maximum amount authorized in the resolution.

This bill would delete that condition.

(5) Existing law authorizes the Treasurer, when the finance committee created by the bond act deems it in the best interests of the state, to issue notes, on a negotiated or a competitive-bid basis, maturing within a period not to exceed 2 years, in anticipation of the sale of bonds.

This bill would increase the maturation date of those notes to 5 years and make related changes.

(6) Existing law specifies the manner in which the Treasurer may sell bonds.

This bill would revise these provisions regarding the competitive sale of bonds and the conditions for bidding in a competitive sale or purchasing in a negotiated sale. The bill would make other conforming and nonsubstantive changes to the bond law.

(7) Existing law allows a finance committee to also provide for the issuance and sale or exchange of refunding bonds for the purpose of redeeming, retiring, or purchasing for retirement, outstanding bonds at or before their maturity, if the committee determines, among other things, that refunding is necessary or advisable to effect a saving in debt service cost to the state.

This bill would require the committee, when making this determination, to include, as interest on a refunded bond, the interest, if any, that will result from a related hedging contract and would authorize the committee, when determining debt service savings, to base the interest of a refunding bond upon the effective fixed interest rate under a hedging contract.

*The people of the State of California do enact as follows:*

SECTION 1. Section 16724.5 of the Government Code is amended to read:

16724.5. (a) (1) For purposes of this section, “revolving fund” means the General Obligation Bond Expense Revolving Fund created pursuant to this section.

(b) There is in the State Treasury the General Obligation Bond Expense Revolving Fund, which shall consist of all money appropriated by the Legislature into that fund or payable into that fund in accordance with this section.

(c) All money in the revolving fund is hereby appropriated and shall be available without regard to fiscal years for all of the following:

(1) The payment of the expenses incurred by the State Treasurer in having the bonds prepared and in advertising their sale or their prior redemption, and of the other costs described in subdivision (e) of Section 16727.

(2) For expenses incurred by the committee pursuant to Section 16758.

(3) For payment for legal services pursuant to Section 16760.

(d) Whenever bonds are sold, out of the first money realized from their sale, there shall be redeposited in the revolving fund the sums that have been expended for the purposes specified in subdivision (c), which may be used for the same purposes and repaid in the same manner whenever additional sales are made.

SEC. 2. Section 16731 of the Government Code is amended to read:

16731. Whenever the committee determines that the sale of all or any part of the bonds authorized to be issued is necessary or desirable, it shall adopt a resolution to that effect. The resolution shall specify all of the following as to the bonds then to be sold:

(a) The aggregate number, aggregate par value, denominations, and the date of the bonds to be then sold. The denominations shall be in the sum of one thousand dollars (\$1,000) or multiples of that sum. The date appearing on the bonds shall be deemed to be the date of issuance for all purposes of this chapter, irrespective of the actual date of delivery of the bonds and the payment of the purchase price of the bonds.

(b) The dates of maturity and the amount of the bonds maturing at each date of maturity, which amounts need not be equal. The last dates of maturity shall be not more than 45 years after the date of the bonds.

(c) Whether or not the bonds are to be subject to redemption or tender prior to maturity, and, if so, the provisions for the redemption or tender, the manner of the call or notice thereof, and the price or prices at which the bonds shall be subject to redemption or tender.

(d) (1) (A) The annual rate, or rates, of interest that the bonds to be issued shall bear, which shall be in the increments determined by the Treasurer, but not in excess of 11 percent. The rate or rates may be determined at the time of the sale of the bonds.

(B) As an alternative to subparagraph (A), the resolution may specify that the bonds may pay a variable interest rate or rates, as prescribed in the resolution, but not in excess of 11 percent per annum, and in accordance with the requirements of this subparagraph.

(i) At the time and as the result of the issuance of any bonds bearing a variable interest rate, the aggregate principal amount of all state general obligation bonds bearing variable interest rates may not exceed 20 percent of the aggregate principal amount of all state general obligation bonds then outstanding.

(ii) For purposes of the calculation made pursuant to clause (i), variable rate bonds shall not include commercial paper notes issued pursuant to Section 16731.6 or bonds that have an effective fixed interest rate through a hedging contract, as specified in subparagraph (C), but shall include bonds that have an effective variable interest rate through a hedging contract.

(iii) Notwithstanding any other provision of this chapter, if the committee decides to issue state general obligation bonds bearing variable interest rates, the committee is not required to comply with Section 16732.

(iv) Notwithstanding any other provision of law, if bonds are issued bearing a variable interest rate under a bond act approved by the voters on or after January 1, 2002, and if the variable interest rate bonds provide a right of tender, then any amount payable by the state as a result of the tender with respect to principal of and interest on the bonds prior to the regularly scheduled principal or interest payment dates, or payable by the state pursuant to redemption or call initiated as a means to repay the obligation of the state resulting from the tender, is backed by the full faith and credit of the state and shall be payable under the bond act.

(v) A contractual obligation of the state to repay advances and pay interest thereon under a credit enhancement or liquidity agreement entered into in connection with variable interest rate bonds providing a right of tender and issued under a bond act approved by the voters on or after January 1, 2002, shall be backed by the full faith and credit of the state and shall be payable under the bond act, except to the extent bond interest paid with an advance and interest on the advance would exceed the maximum interest rate specified in this subdivision.

(C) For the purposes of clause (ii) of subparagraph (B), bonds that have an “effective fixed interest rate through a hedging contract” means bonds for which the Treasurer determines the hedging contract meets either of the following conditions:

(i) Significantly reduces variable rate risk by providing changes in fair values or cashflows that substantially offset the changes in fair value or cashflows of the bonds.

(ii) Qualifies for integration with the bonds in calculating the yield on the bonds under the rules prescribed in Section 148 of the United States Internal Revenue Code (26 U.S.C. Sec. 148).

(D) The Treasurer’s determination specified in subparagraph (C) shall be made at the time the hedging contract is entered into and shall apply through the maturity of the bonds, unless the hedging contract is terminated prior to maturity.

(2) (A) (i) Notwithstanding any other provision of law, for bonds approved by the voters after January 1, 2006, payment of any amounts owed by the state to a counterparty, after any offset for payments owed to the state on any hedging contract described in Section 5922 in connection with those bonds, shall be deemed to be included within the appropriation for interest on the bonds contained in the applicable bond act.

(ii) The total payments of stated interest on the bonds together with payments owed by the state after any offset for payments owed to the state

on a hedging contract shall not exceed the maximum interest rate set forth in this subdivision.

(iii) To the extent payments of interest on a bond, together with payments on a hedging contract, would, in any fiscal year, exceed the maximum interest rate specified in this subdivision, the excess amounts may be paid in subsequent fiscal years, if the aggregate amount of interest and that excess amount paid in any year does not exceed the maximum interest rate specified in this subdivision.

(B) The Treasurer may not enter into any hedging contract described by subparagraph (A) unless the committee has approved policies developed by the Treasurer relating to the entering into and managing of those hedging contracts that shall include both of the following:

(i) A requirement that any hedging contract or program of contracts is designed to reduce the amount or duration of payment, currency, rate, spread, or similar risk or result in a lower cost of borrowing when used in combination with the issuance or carrying of bonds.

(ii) A description of the criteria to be used to evaluate the potential risks and benefits to the state of entering into a particular hedging contract or program of contracts and to evaluate the performance of outstanding hedging contracts in comparison to the objectives for which the hedging contract was executed.

(C) The policies approved pursuant to subparagraph (B) are exempt from the requirements of Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3.

(e) The interest payment dates.

(f) The technical form and language of the bonds.

(g) Whether or not the right is reserved to make delivery in the form of temporary or interim bonds, certificates, or receipts, exchangeable for definitive bonds when executed and available for delivery. If the right is reserved, the denominations and form of the temporary securities shall be stated.

(h) Provisions for the registration and exchange of bonds and for the use of a depository to hold book-entry bonds after issuance.

(i) All other terms and conditions of the bonds and of the execution, issuance, and sale of the bonds, which shall be consistent with all of this chapter.

SEC. 3. Section 16731.6 of the Government Code is amended to read:

16731.6. (a) Notwithstanding any other provision of this chapter, and as an alternative to the procedures set forth in Section 16731, the committee may provide for the issuance of all or part of the bonds authorized to be issued as commercial paper notes. The committee shall adopt a resolution finding that issuance of the bonds in the form of commercial paper notes is necessary and desirable, directing the Treasurer to arrange for preparation of the requisite number of suitable notes, and specifying other provisions relating to the commercial paper notes, including all of the following:

(1) For each program of commercial paper notes authorized, the resolution shall contain the final date of maturity and the total aggregate principal

amount of the commercial paper notes authorized to be outstanding at any one time up to the maturity date, in accordance with all of the following:

(A) The resolution may provide that the commercial paper notes may be issued and renewed from time to time until the final maturity date, and that the amount issued from time to time may be set by the Treasurer up to the maximum amount authorized to be outstanding at any one time.

(B) The resolution shall include methods of setting the dates, numbers, and denominations of the commercial paper notes.

(C) The determination of the final maturity date and total amount by the committee shall be made upon recommendation of the Treasurer to meet the needs of the state for funds, to provide the maximum benefit to potential purchasers, and to respond to the expected demand for the commercial paper notes.

(D) Notwithstanding any other provision of this chapter, whenever the committee determines to issue commercial paper notes, the committee is not required to comply with the requirements of Section 16732.

(2) The method of setting the interest rates and interest payment dates applicable to the commercial paper notes, in accordance with the following:

(A) Commercial paper notes may bear a stated rate of interest payable only at maturity, which rate or rates may be determined at the time of sale of each unit of commercial paper notes.

(B) The rate of interest borne by the commercial paper notes shall not exceed 11 percent per annum.

(C) Notwithstanding any other provision of this chapter, whenever the committee determines to issue commercial paper notes, the committee is not required to comply with the requirements of Section 16733.

(3) Any provisions for the redemption of the commercial paper notes prior to stated maturity.

(4) The technical form and language of the commercial paper notes.

(5) All other terms and conditions of the commercial paper notes and of their execution, issuance, and sale, deemed necessary and appropriate by the committee.

(b) Notwithstanding any other provision of this chapter, when the committee determines to issue commercial paper notes, all of the following shall apply:

(1) The commercial paper notes may be sold at negotiated sale at a price below the par value in a manner consistent with paragraph (2) of subdivision (a).

(2) During the term of any program of commercial paper notes, the renewal and reissuance from time to time of the commercial paper notes in an amount up to the maximum amount authorized by the resolution shall be deemed to be a refunding of the previously maturing amount, permitted by and consistent with Article 6 (commencing with Section 16780).

(3) Consistent with the intent for the General Fund to realize a savings in debt service costs when commercial paper notes are issued in place of bonds without shifting or adding financing and debt service costs to the bond funds, the state administrative costs of commercial paper and interest

payable and other costs associated with commercial paper notes shall be paid for as follows:

(A) The proceeds of commercial paper notes are, notwithstanding Section 13340, continuously appropriated to pay the state administrative costs of commercial paper including, but not limited to, costs of the Treasurer's office, the Controller's office, and the Department of Finance.

(B) The interest payable on maturing commercial paper notes and other costs associated with commercial paper notes not specified in paragraph (A), including, but not limited to, remarketing fees, issuing and paying agent fees, the letter or line of credit provider fees, the rating agency fees, and bond counsel fees, shall be paid from the General Fund which, notwithstanding Section 13340, is continuously appropriated to pay the interests and costs.

SEC. 4. Section 16735 of the Government Code is amended to read:

16735. Each bond shall contain a reference to the bond act, and if subject to call, tender, or redemption prior to maturity, a recital to that effect.

SEC. 5. Section 16736 of the Government Code is repealed.

SEC. 6. Section 16737 of the Government Code is amended to read:

16737. (a) When the committee deems it in the best interests of the state, it may authorize the Treasurer, upon those terms and conditions that may be fixed by the committee or determined by the Treasurer, to issue notes, on a negotiated or a competitive-bid basis, maturing within a period not to exceed five years, in anticipation of the sale of bonds duly authorized at the time the notes are issued. The proceeds from the sale of those notes shall be deposited in the related fund and used only for the purposes for which may be used the proceeds of the sale of bonds in anticipation whereof the notes were issued or as additionally authorized by this section.

(b) The notes authorized by this section may be sold at a price at, above, or below the principal amount thereof, at the discretion of the Treasurer.

(c) Any premium received from the sale of notes authorized by this section may be applied to pay costs of issuance of the notes or interest accruing on the notes.

(d) The notes authorized by this section may bear a fixed or variable rate or rates of interest.

(e) In connection with the sale of notes pursuant to this section, the Treasurer may engage the services of legal and financial advisers, credit enhancers, trustees or paying agents, and other professionals that the Treasurer deems necessary, and may enter into contracts for these services, to be paid from proceeds of the notes or any duly enacted appropriation.

(f) When the committee deems it in the best interests of the state, it may authorize the Treasurer to deliver the notes in payment for work or material furnished to the state for a public improvement, pursuant to a contract awarded in the manner prescribed by law. The notes shall be so delivered only for the purposes for which may be used the proceeds of the sale of bonds in anticipation whereof the notes were issued.

(g) All notes issued pursuant to this section and any renewals thereof shall be payable at a fixed time, solely from the proceeds of the sale of the

bonds and not otherwise, except if the sale of the bonds did not occur prior to the maturity of the notes issued in anticipation of the sale, the Treasurer shall, in order to meet the notes or the renewals thereof then maturing, issue renewal notes for this purpose. No renewal of a note or a renewal note shall be issued after the sale of bonds in anticipation of which the original note was issued.

(h) Every note issued pursuant to this section and any renewal thereof shall, unless paid from a renewal note, be payable from the proceeds of the sale of bonds and not otherwise. The total amount of the notes or renewals thereof issued and outstanding shall not exceed the total amount of the unsold bonds.

(i) Interest on the notes issued pursuant to this section shall be payable from any appropriation made for that purpose or from proceeds of the sale of the notes.

SEC. 7. Section 16752 of the Government Code is amended to read:

16752. The Treasurer may from time to time, by electronic means or by public announcement at the place and at or before the time fixed for a competitive sale of bonds, continue the sale to the time and place the Treasurer may select.

SEC. 8. Section 16752.1 of the Government Code is amended to read:

16752.1. The Treasurer may cancel or postpone a competitive sale of bonds to an indefinite date by public announcement, including by electronic means, made prior to or at the time and place fixed for the sale of the bonds. The Treasurer may give notice of the new time and place of the sale of the bonds that the Treasurer may deem advisable.

SEC. 9. Section 16753 of the Government Code is amended to read:

16753. (a) Each bid at a competitive sale shall be submitted to the Treasurer in the form and by the means specified by the Treasurer by public announcement.

(b) Each proposal for purchase of bonds in a negotiated sale shall be made in a bond purchase contract or similar agreement approved by the Treasurer.

(c) (1) The Treasurer shall require that each bidder in a competitive sale or underwriter in a negotiated sale provide a good faith deposit of at least one-half of 1 percent of the principal amount of the bonds for which the bidder or underwriter submits a bid or proposal. The good faith deposit shall be based upon the principal amount of bonds offered for sale in the amount that has been publicly announced at least one day prior to receipt of bids for a competitive sale, or in the amount that is reasonably determined by the Treasurer at least one day prior to a negotiated sale of bonds. The Treasurer shall specify the form of the deposit, which may be a cashier's check, a surety bond, a wire transfer of funds, or a combination thereof. The deposit shall not bear interest.

(2) This subdivision shall apply only to bonds sold with a fixed interest rate.

SEC. 10. Section 16754 of the Government Code is amended to read:



16754. (a) The bonds specified in the resolution shall be sold by the Treasurer, at the time fixed by the Treasurer, and upon the notice that the Treasurer may deem advisable, or at the time to which the sale shall have been so continued, at a competitive sale to the bidder whose bid will result in the lowest interest cost on account of those bonds.

(b) The Treasurer shall reject any and all bids for the bonds that shall be below the par value thereof plus the interest that shall have accrued thereon from the date thereof or, if any past due coupon or coupons have been detached from the bonds prior to the delivery thereof, then from the due date of the latest coupon so detached, to the date of the purchaser's payment for the bond.

(c) The method of determining the lowest interest cost bid shall be prescribed in the bond resolution and shall be limited to either the net interest cost method or the present worth basis method, also referred to as the true interest cost, bond book basis, and Canadian interest cost method.

(1) The net interest cost of each bid shall be determined by ascertaining the total amount of interest that the state would be required to pay under that bid, from the date of the bonds to the respective maturity dates of the bonds then offered for sale, at the coupon rate or rates specified in the bid, less the total amount of the premium, if any, offered by the bid. The bid under which the amount so ascertained is the least shall be deemed to be the bid resulting in the lowest net interest cost.

(2) Under the present worth basis method, the bonds shall be awarded to the bidder submitting the lowest interest rate bid, which shall be determined by doubling the semiannual interest rate, compounded semiannually, necessary to discount the debt service payments to the specified interest computation date and to the price bid.

(d) Under either method specified in subdivision (c), the sale shall be for cash, payable upon the delivery of the bonds in definitive form, or if the right to deliver temporary securities has been reserved, then upon the delivery of the temporary securities.

SEC. 11. Section 16754.3 of the Government Code is amended to read:

16754.3. (a) The bonds specified in the resolution shall be sold by the Treasurer, at the time fixed by the Treasurer, and upon the notice that the Treasurer may deem advisable, or at the time to which the sale shall have been so continued, either at a competitive sale to the bidder whose bid will result in the lowest interest cost on account of those bonds or by a negotiated sale if the Treasurer determines it will result in a lower interest cost. With respect to bonds sold by the Treasurer by negotiated sales, the Treasurer shall make a finding on the public record as to why a competitive sale was not used. The Treasurer may sell the bonds at a price below the par value thereof, but the discount on bonds so sold shall not exceed 3 percent of the par value. The interest, if any, accrued to the date of delivery of, and payment for, the bonds shall be added to the sale price of the bonds in any case.

(b) (1) The method of determining the lowest interest cost bid shall be prescribed in the bond resolution and shall be limited to either the net interest cost method or the true interest cost method.

(A) The net interest cost of each bid shall be determined by ascertaining the total amount of interest that the state would be required to pay under that bid, from the date of the bonds to the respective maturity dates of the bonds then offered for sale, at the interest rate or rates specified in the bid, less the total amount of the premium, if any, or plus the total amount of the discount, if any, offered by the bid. The bid under which the amount so ascertained is the least shall be deemed to be the bid resulting in the lowest net interest cost.

(B) Under the true interest cost method, the bonds shall be awarded to the bidder submitting the lowest interest rate bid determined by the nominal interest rate that, when compounded semiannually and used to discount the debt service payments on the bonds to the date of the bonds, results in an amount equal to the price bid for the bonds, excluding interest accrued to the date of delivery.

(2) Under either method specified in this subdivision, the sale shall be for cash, payable upon the delivery of the bonds in definitive form, or if the right to deliver temporary securities has been reserved, then upon the delivery of the temporary securities.

(c) Notwithstanding subdivision (a) or (b), if the resolution prescribes that the bonds may pay a variable interest rate, as specified in subdivision (d) of Section 16731, the Treasurer may sell the bonds by negotiated sales if the Treasurer determines that it is in the best interest of the state to do so.

(d) This section shall apply to any bonds authorized at any statewide election held at any time after the effective date of this section. Section 16754 shall apply only to bonds authorized at elections held before the effective date of this section.

SEC. 12. Section 16755 of the Government Code is amended to read:

16755. (a) The deposit of each unsuccessful bidder shall be returned to the bidder promptly upon the rejection of the bidder's bid or the acceptance of another bid.

(b) The deposit of the successful bidder or underwriter in a negotiated sale shall, immediately upon the acceptance of the bid or proposal, become and be the property of the state, be placed in the State Treasury to the credit of the fund, and be credited to the successful bidder or underwriter upon the purchase price of the bonds when the purchase price is paid in full within the time mutually agreed upon between the successful bidder or underwriter and the Treasurer.

(c) If the purchase price is not paid in accordance with subdivision (b), the successful bidder or underwriter shall have no right in and to the bonds by reason of the bid or purchase contract and the successful bidder or underwriter shall not have any right to the recovery of the deposit accompanying the bid or purchase contract or to any allowance or credit by reason of that deposit unless it shall appear that the bonds cannot be validly issued or delivered, or unless the return of the good faith deposit to the underwriter is provided for in the purchase contract.

SEC. 13. Section 16757 of the Government Code is amended to read:

16757. (a) The proceeds of each sale of bonds, and the amount that may have been paid as accrued interest on the bonds, shall be forthwith paid over by the Treasurer into the fund.

(b) All money deposited in the fund pursuant to this section that is derived from premium and accrued interest on bonds sold shall be reserved in the fund and shall be available for transfer to the General Fund as provided in the bond act, except that amounts derived from premium on the bonds may be used to pay costs of issuance of the bonds, as provided in Section 16724.5, and in subdivisions (d) and (e) of Section 16727, prior to transfer to the General Fund.

SEC. 14. Section 16780 of the Government Code is amended to read:

16780. (a) The committee may provide for the issuance and sale or exchange of refunding bonds for the purpose of redeeming, retiring, or purchasing for retirement, outstanding bonds at or before their maturity, if the committee determines that refunding is necessary or advisable in order to do either of the following:

(1) To effect a favorable reorganization of the debt structure of the state.

(2) To effect a saving in debt service cost to the state, as measured by the present value of that saving.

(b) When determining debt service savings for purposes of paragraph (2) of subdivision (a), the committee shall include, as interest on a refunded bond, the interest, if any, that will result from a related hedging contract, as described in subparagraph (A) of paragraph (2) of subdivision (d) of Section 16731. The committee may, when determining debt service savings, for purposes of paragraph (2) of subdivision (a), base the interest of a refunding bond upon the effective fixed interest rate under a hedging contract described in clause (ii) of subparagraph (B) of paragraph (1) of subdivision (d) of Section 16731.